

Thank you for inviting me to share with you an update on the activities of the Kentucky Public Service Commission and my thoughts on the future direction of the PSC.

Before I begin, let me take note of one important point. Because Kenergy has or soon will have matters pending before the PSC, I cannot and will not speak specifically about Kenergy or, for that matter, any other issues currently before the PSC or in which the PSC is involved through litigation. Nor can I answer any questions about such matters. I would ask your indulgence in this.

It has been an interesting first six months for me in Frankfort. When I took office in February, arriving from a small town law practice, it was just a few weeks into a new administration, the legislature was in session, and there were several major pieces of litigation pending in the Federal Courts and at the Federal Energy Regulatory Commission involving the PSC. I had virtually no experience with your industry, and only a general understanding of its importance to our Commonwealth. It was a real baptism by fire. And it has only gotten warmer since then.

One of the first things I learned was that what I do at the PSC affects each and every citizen of Kentucky, with the exception of a few survivalists in Eastern Kentucky. That is a tremendous responsibility – one that requires the PSC and its staff to do their work with the utmost integrity, transparency and accountability.

That is certainly the standard that Vice Chairman Ellen Williams and I have set for ourselves and for the employees of the PSC. As you well know, the PSC is fortunate to have an extremely and very dedicated professional staff that possesses a truly remarkable amount of institutional knowledge. Ellen and I have enjoyed getting to know them and have come to rely on them.

One of the challenges of any government transition is to keep moving forward without losing momentum. The PSC has been able to do that because of the exceptional leaders that have joined our staff.

Our new Executive Director, Beth O'Donnell, joined us in May. A Kentucky native, she comes to us with a wealth of experience in utility regulation, having served as an administrative law judge for the Missouri Public Service Commission and as a senior attorney for the Illinois Power Company. Beth quickly earned the confidence of the staff and Ellen and I have come to rely on her a great deal.

Beth's second-in-command is a familiar face. Bob Amato has stepped up from director of engineering – where he served capably for a number of years – to become the deputy executive director. We expect to name a new engineering director very soon.

Jason Bentley joined us in late June as general counsel. Jason is returning to Kentucky from that dark region known as “Inside the Beltway.” Of course, I'm referring to Washington, DC. We are glad he's seen the light and returned to the Bluegrass. Jason's experience

as a staff member for the House Energy and Commerce Committee will be invaluable to us in our dealing with the Federal Energy Regulatory Commission, Congress and other federal policy-making bodies.

Another key addition to the PSC staff is Garnett Thurman. Many of you may know him from his service at the Legislative Research Commission in Frankfort, where he served the House minority leadership and also dealt with energy issues. Garnett is our link to the General Assembly and also is helping us build stronger relationships with local governments across the Commonwealth.

You may see some additional changes and some more new faces in the coming months. Rest assured that it will not be change simply for the sake of change. I certainly subscribe to the common adage that “if it ain’t broke, don’t fix it.” Our goal – as it is throughout Governor Fletcher’s administration – is to make your state government work harder, smarter and more efficiently. Where we can implement changes that will make the PSC do a better job for regulated utilities and their customers, we intend to do so. If you have ideas for improvement, I encourage you to share them with us.

One thing that will not change is the PSC’s core mission: to insure that utilities receive fair, just and reasonable rates and that their customers receive adequate service. That requires us to balance three factors:

- Keeping rates as low as possible
- Ensuring customers receive adequate, safe and reliable service
- Maintaining financially healthy utilities, be they investor owned or cooperatives

In the arena of electricity, the balancing act in Kentucky occurs against a national backdrop of an industry that, in recent years, has been in flux and, in some cases, in trouble. Fortunately, the most serious problems have not extended into Kentucky. As PSC chairman, I intend to see that it stays that way.

In two days, it will be one year since the largest blackout in our nation's history. We remember it as the day the lights went out in many neighboring or nearby states – and stayed on in Kentucky.

I believe that the lights stayed on in Kentucky for a reason. It was because Kentucky's regulated utilities, with the encouragement and support of the PSC, invested wisely and created a system that has proven itself to be robust and dependable. Kentuckians have not had to worry about widespread outages caused by systemic weaknesses. But that does not mean we can afford to be complacent.

In the wake of last year's blackout, the PSC and Kentucky's utilities joined to study the strength of our transmission system. We anticipate that study will be completed soon, and I am hopeful that it will confirm

that our transmission system is deserving of our continued confidence.

Kentucky also is in an enviable position with respect to electric generation facilities. For the most part, we have ample capacity, and utility companies, including the generation and transmission cooperatives, have made the investments necessary to maintain comfortable reserve margins. We need to continue our long-range planning efforts to ensure that we never find ourselves in a situation in which our generating capacity is not adequate to meet native load requirements and we become dependent on other states whose interests are unlikely to coincide with ours.

The challenge of maintaining a reliable electric infrastructure ties into the other major policy issue facing Kentucky – the question of regionalization of electric transmission facilities and electricity markets.

As you well know, it has not always been easy to reconcile Kentucky's positions on these issues with those of some other states or with the Federal Energy Regulatory Commission. Finding the right role for Kentucky in integrated regional transmission systems will continue to be a major focus of our work at the PSC.

We recently took a major step forward in that area by settling the question of whether Kentucky Power – American Electric Power's Kentucky operating unit – ought to become a member of the PJM

Interconnection regional transmission organization. The agreement reached in that case accomplished several important goals:

- It protected the interests of Kentucky Power's native-load customers
- It met the needs of both AEP and PJM as the utility integrates its transmission system with the regional grid operator
- Finally, it allowed us to settle the case brought against Kentucky by the Federal Energy Regulatory Commission in a way that did not compromise the regulatory authority of the PSC, which I believe inures to the substantial benefit of Kentucky ratepayers.

The larger issue of electric industry restructuring and regionalization remains with us. But I believe that events of the past year have changed the debate in a number of very significant ways.

First, the blackout brought the swift realization that creating broader electric markets is of little use or consequence if the transmission infrastructure is incapable of moving electrons to meet market demands. That recognition has rightly shifted the focus – both in Washington and elsewhere – to reliability, rather than restructuring.

Second, the Federal Energy Regulatory Commission's push toward industry restructuring has been slowed by the vigorous skepticism expressed by Congressional delegations and governors from many states, including Kentucky.

Third, a number of factors – a general economic slowdown which is just now ending, an abundance of generating capacity, particularly in the Southeast, and concerns about the operation of the transmission grid and the transparency of electricity markets - have brought the merchant power industry nearly to a standstill and have thus removed one of the strongest imperatives for restructuring electricity markets.

That in turn has meant that the so-called “old way” of doing business in the electric utility industry – vertically integrated utility companies subject to reasonable state regulation – is again finding favor in the eyes of consumers, financial markets and policy-makers alike.

The “old way” has served Kentucky well. Not only is our electric system reliable, but we enjoy some of the lowest electric rates in the nation. But that does not mean that Kentucky rejects regionalization.

Kentucky’s position with respect to regionalization has consistently rested on certain bedrock principles:

- The Kentucky PSC has consistently supported the creation of regional entities in order to improve the reliability, stability and flexibility of the transmission system.
- If regional transmission facilities are improved in order to facilitate the long-distance transport of electricity, the costs of the improvement should be borne by the beneficiaries of the services, i.e. the cost-causers, and not by the native-load ratepayers.

- Membership in a regional transmission organization should not be detrimental to Kentucky consumers, either with respect to preserving the priority of native loads – as required by Kentucky statute – or with respect to maintaining Kentucky’s low electric rates. Kentucky residents and businesses should not be asked to pay more for electricity so that residents and businesses in other states can pay less.

It has not always been easy to reconcile Kentucky’s positions on these issues with those of some other states or with the Federal Energy Regulatory Commission. Finding the right role for Kentucky in integrated regional transmission systems will continue to be a major focus of our work at the PSC. I believe we are making progress in that regard.

Finally, let me address a topic that has been much on my mind in recent weeks. On this issue there can be no compromise.

When he took office, Governor Fletcher pledged to restore trust and faith and confidence in state government. Every state employee – whether appointed by this or previous administrations – has the same obligation.



The Kentucky Public Service Commission has a reputation for integrity and accountability. Nothing I have seen in my time at the PSC has caused me to believe that reputation is anything other than well deserved. The members of the PSC staff do not take lightly the obligations that come with being a public servant and do their utmost to meet those obligations. They take justifiable pride in their work and in their agency.

That said, there is always room for improvement. From our first days in office, Ellen Williams, Beth O'Donnell and I have looked for ways to do things better – better for regulated utilities, better for consumers, better for PSC employees.

The most important improvements we can make are in the areas of integrity, accountability and transparency – to take that high level which we already achieve and to set the bar ever higher, to challenge and push ourselves to do even better.

We already have instituted a number of changes. Some I hope will soon become apparent to you, as we implement procedures that will make the PSC more efficient and more responsive to utilities and customers alike.

Other changes may be less visible, but no less important. We are reviewing all of our procedures to insure that the actions of the PSC and its employees adhere to the highest standards. That does not mean that every party to every case will agree with every decision. But it does mean that every decision should and will be made in a manner that is open, fair and beyond reproach – and that inspires public trust.

The effectiveness of the PSC rests in large measure in the confidence placed in us by the Governor who appoints us, the legislators who enact the laws we implement, the utilities we regulate and, most importantly, the citizens of this Commonwealth. As chairman, I have no duty more important than ensuring that the PSC, through the work we do and the decisions we make, continues to earn that confidence each and every day.

In closing, I appreciate having this opportunity to meet with you and to learn more about Kenergy and its customers. I look forward to working with you in the coming months and years. Thank you very much.